

***United States Court of Appeals
for the Second Circuit***

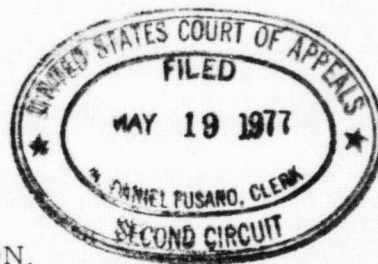


**APPELLANT'S
REPLY BRIEF**

77-6012

UNITED STATES COURT OF APPEALS

for the
SECOND CIRCUIT



SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellee-Appellant,

-against-

PARKLANE HOSIERY CO., INC.
HERBERT N. SOMEKH,

Defendants-Appellants-Appellees.

ON APPEAL AND CROSS-APPEAL FROM THE UNITED STATES
DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK

REPLY BRIEF FOR
PARKLANE HOSIERY CO., INC. AND HERBERT N. SOMEKH

JACOBS PERSINGER & PARKER
Attorneys for Defendants-Appellants-Appellees
Parklane Hosiery Co., Inc. and Herbert N. Somekh
70 Pine Street
New York, New York 10005
(212) 344-1866

IRVING PARKER
JOSEPH N. SALOMON
JEFFREY I. SLONIM

Of Counsel

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The Reply

Upon a truncated version of the record, the answering brief of the Securities and Exchange Commission ("SEC") mistakenly contends that the findings below of three deficiencies in the pre-merger proxy statement ("Proxy Statement") (A504) of Parklane Hosiery Company, Inc. ("Parklane") were not "clearly erroneous", and, therefore, should not be reversed. To that contention, the short

answer is that each of those findings was made in total disregard of certain relevant testimony of the SEC's own witnesses elicited (a) upon cross-examination at trial and (b) during the SEC's investigation -- testimony which established that the three findings made were clearly erroneous.* More particularly, the significant relevant facts which the Court below inexplicably ignored and the SEC's briefs have correspondingly avoided appear in defendants' main and answering briefs.** Other such significant facts appear herein.

In contrast to the Opinion below, upon appeal the entire evidence must be considered in determining the question whether the findings were clearly erroneous.

* At trial, the SEC called four witnesses in all, other than defendant Herbert N. Somekh ("Somekh"). The four were Thomas E. Baggott, a vice president of Bankers Trust Company ("Bankers Trust") (A60), Richard D. Tunick, an assistant vice president of National Bank of North America (A320), Robert S. Curtiss, a self-employed real estate counselor (A335), and Peter A. Russ, who had been employed by Thomson & McKinnon Auchincloss Kohlmeyer, Inc. ("Thomson & McKinnon") (A301-302). As to those witnesses, the respects in which the District Court disregarded testimony on cross-examination and testimony given during the SEC investigation are set forth in detail in defendants' main brief and in their answering brief on the SEC's cross-appeal. Others appear herein.

** References to pages of the SEC's answering brief appear herein as "(SEC ans. br.)"; references to pages of defendants' main brief on this appeal appear herein as "(Ds' main br.)"; references to pages of the SEC's opening brief on its cross-appeal appear herein as "(SEC main br.)"; references to pages of defendants' answering brief on the SEC's cross-appeal appear herein as "(Ds' ans. br.)"; references to pages of the Appendix appear herein as "(A)."

United States v. United States Gypsum Co., 333 U.S. 364 (1948); Feder v. Martin Marietta Corp., 406 F.2d 260 (2d Cir. 1969), cert. denied, 396 U.S. 1036 (1970). In United States Gypsum, the Supreme Court wrote:

"The practice in equity prior to the present Rules of Civil Procedure was that the findings of the trial court, when dependent upon oral testimony where the candor and credibility of the witnesses would best be judged, had great weight with the appellate court. The findings were never conclusive, however. A finding is 'clearly erroneous' when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed." 333 U.S. at 395. (footnote omitted) (emphasis added)

Here, there is no impediment to reversal; rather there are strong and compelling reasons for it, particularly in view of the failure of the Court below to give effect to the testimony on cross-examination of the very same witnesses upon whose direct testimony it chose to rely.*

We now turn to the SEC's answering brief which,

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* The SEC incorrectly asserts that defendants, by their appeal, are seeking "to retry the case" (SEC ans. br. 3). To the contrary, defendants seek to have the case as tried reviewed on the basis of the entire record and not only on the part of it reflected in the Opinion below and the SEC's briefs.

in the use of terms descriptively befitting it, charges, but fails to show as a matter of fact or law, that defendant Somekh conceived and successfully executed a plan "to eliminate - by fraudulent and deceptive means - the public shareholders of the corporate defendant he controlled" (SEC ans. br. 1).

There was no fraud or deception, as a matter of fact or law, in returning Parklane to its private status. The Proxy Statement expressly states (a) that the purpose for the merger was to return Parklane to its private status, thereby eliminating the public shareholders (A506), and (b) that, upon the merger, only the shareholders of the surviving corporation would be "entitled to the benefit of all of the assets, earnings, earning capacity and cash flow of the Company" (A507).

As was seen in defendants' main and answering briefs, and as will hereinafter be seen, the use to be made of those assets -- even if it were to enable Somekh to repay a personal indebtedness -- was of no concern to the public shareholders. The use to be made of those assets after the merger was immaterial, and, in this regard, the District Court made no contrary finding.

I

The SEC's answering brief (p. 10) has finally acknowledged that any disclosure as to the use which may be made of a company's assets upon its return to private status has no relevance or materiality under the federal securities laws. Thus, the SEC's answering brief (p. 10) states: "[O]f course a private owner may deal with his company as he sees fit." (emphasis added) As defendants' main brief (p. 48) stated -- and the SEC has not denied -- "It could have made no difference to the minority shareholders whether or not the 'overriding purpose' of the merger was to enable Somekh to pay a personal indebtedness or to have gifted the Parklane assets to charity or to have used those assets in any other way." (emphasis added)

Once the Proxy Statement disclosed, as it did here, (a) that "[t]he proposed merger is intended to restore the Company to the status of a privately held company" (A506) and (b) that if the proposed merger were consummated the shareholders of the surviving corporation would be entitled to the benefit of all its assets (A507), all that had to be disclosed was disclosed.

While the Court below, nevertheless, found the "overriding purpose for the merger was to enable Somekh to repay his personal indebtedness" and that such purpose was

not disclosed in the Proxy Statement (A13), neither the Court below nor the SEC have shown -- nor could they -- that, in light of the disclosures made, the "overriding purpose" was, in the language of Rule 14a-9, a "material fact necessary in order to make the statements [in the Proxy Statement] not false or misleading."* (See Ds' main br. 46-50) Rather, the Court below, recognizing that materiality of a fact is a "separate question" from the question of its non-disclosure (A13), made no finding that non-disclosure of the "overriding purpose" for the merger was material. Thus, there was no basis upon which the District Court could have granted relief in respect of the purpose for the merger. It was clearly erroneous in doing so.

Significantly, in Lessler v. Dominion Textile Limited, 411 F. Supp. 40 (S.D.N.Y. 1975), Judge Duffy had found that the very disclosure made in the Proxy Statement here was adequate. Thus, in Lessler, the Court wrote:

"Equally meritless is the charge that the Information Statement does not set forth a valid business purpose for the merger. On the contrary, it discloses that Newco was formed solely for the merger and that the simple result of the merger will be the 100% ownership of DHJ by Dominion." 411 F. Supp. at 42.

*Rule 14a-9, 17 C.F.R. § 240.14a-9, is reproduced in defendants' main brief at page 70.

Similarly, in Santa Fe Industries, Inc. v. Green, ___ U.S. ___, 45 U.S.L.W. 4317, 4322 n.2 (March 23, 1977) (Stevens, J., concurring), Mr. Justice Stevens flatly rejected the SEC's contention here of relevance or materiality as to the "overriding purpose" for the merger. Mr. Justice Stevens wrote:

"The motivation for the merger is a matter of indifference to the minority stockholders because they retain no interest in the corporation after the merger is consummated."

The SEC here has not in any respect whatsoever attempted to respond to the holding in Lessler, supra, or the corresponding statement of Mr. Justice Stevens in Santa Fe, supra.^{*} Rather, the SEC is actually in accord with both of them in stating that "of course a private owner may deal with his company as he sees fit" (SEC ans. br. 10). The "overriding purpose" for the merger is a matter of indifference to the minority shareholders for the very reason they do not retain any interest in the surviving corporation as a private company.

^{*}Santa Fe Industries, Inc. v. Green, supra and Lessler v. Dominion Textile Limited, supra are discussed in defendants' main and answering briefs at pages 43-45 and 49-50, respectively.

II

It is now appropriate to lay finally to rest the ghost of the SEC's case on the question whether the so-called "overriding purpose" was relevant and material, and, if so, whether, in light of the disclosures made, the Proxy Statement failed adequately to disclose it. On this issue, the SEC succeeded below, but never should have. The SEC was permitted to inject totally irrelevant and immaterial matter into the proceeding and succeeded in diverting the Court below from the simple fact that Somekh's indebtedness had nothing to do with the federal securities laws and could not have brought about a violation of those laws where it did not otherwise exist.

As will now be seen, the fallacy of the SEC's position and of the corresponding finding made below is clear.

The SEC has not challenged, and the Court below did not question, (a) Parklane's right to return to its private status, or (b) the right of Parklane's majority shareholders to the benefit of all of the company's assets after the merger, or (c) the related disclosures set forth in the Proxy Statement. In short, upon the basis of such disclosures made in the Proxy Statement, neither the SEC nor the minority shareholders had any basis for complaint under the federal securities laws. Neither the SEC nor the Court below has even so much as suggested the contrary.

Rather, as the Court below ruled, "the sole question facing a minority shareholder was whether to accept the \$2.00 per share price or to pursue his rights as a dissenting shareholder in an appraisal proceeding" (A20).^{*} That choice and the amount which the minority shareholder would receive could not have been altered one whit by the fact that Somekh might have been as rich as Croesus or as poor as a church mouse. Nor could the amount a minority shareholder would receive for his shares have been any different even if Somekh sought to return Parklane to its private status so that its assets could be used to create a

^{*} It is apparent that the SEC has not even understood this ruling below. The SEC's misunderstanding of the facts and law in this case and the position of defendants on this appeal appears in the following statement:

"[T]he logic of the defendants' position would lead to the conclusion that no information could ever be material in situations where the person soliciting the proxy controlled the ultimate outcome of the vote." (SEC ans. br. 14)

That statement is patently erroneous. It is not a correct statement of defendants' position. Defendants contend that where, as here, a shareholder is called upon to make a choice between accepting an offering price or exercising appraisal rights, there is material information to be disclosed, as it was, namely, information relevant to the value of the shares to be purchased or appraised. See Santa Fe Industries, Inc. v. Green, supra.

charitable foundation or to purchase, as it did, real estate interests.

For the minority shareholder faced with the prospect of elimination from the public company, his sole interest could have been only to realize fair value for his shares. He could not be less concerned as to whether Somekh was rich or poor, feeble or well, tall or short, or whether he had one or more bank loans or none, or what the amount of the bank loans might have been, or whether he had sufficient assets to repay them.

The SEC's case is based upon the hollow use it was permitted to make of the fact that in the Spring of 1974 Somekh had an interest in three bank loans and that their repayment or reduction was then under consideration. The SEC was blind to all other considerations. It cared nothing for the fact that insofar as the federal securities laws were concerned, Somekh, as the principal shareholder, had the right to influence the decision to have Parklane return to its private status, and, upon the merger, the majority shareholders had the sole right to the benefit of all of the company's assets. Rather, the SEC was so intent upon exacting a penalty based upon the existence of the three bank loans that it did not even attempt to ascertain whether

Somekh had the personal assets to pay them.*

The SEC's sole concern below was to try to prove the fact -- irrelevant and immaterial to the minority shareholders and the federal securities laws -- that, after the merger, Somekh contemplated the sale of, and did sell, real estate interests he owned to Parklane; that he was to, and did, receive payment therefor from Parklane; and that he intended to, and did, use some of the proceeds from such sales to repay or reduce his bank loans. The SEC was successful in its endeavor below. The SEC achieved its result in a decision which demonstrably is internally incon-

* While it has been seen that the Somekh assets -- amounting to more than \$4,000,000 -- were far greater than the amount of the three bank loans (Ds' main br. 15-16), the SEC's answering brief asserts that such assets were not "current" assets (p. 6) or were only assets "on paper" (p. 9). Even if this were relevant, such characterizations are certainly not warranted by the record. In fact, Baggott, of Bankers Trust, which was the principal creditor of the Somekhs, to the extent of \$900,000, testified that the loan was secured by a "security package" valued at more than \$2,000,000 and that it was to that collateral that Bankers Trust looked for repayment of the loan "when, as and if" repayment was to be made (Ds' main br. 16-17; Ds' ans. br. 15).

Furthermore, the SEC's statement (SEC ans. br. 9) that Somekh did not liquidate any of his assets to repay his loans is but another example of an inaccurate and needlessly misleading statement torn out of context. That statement is based upon a letter to Bankers Trust dated April 25, 1975 (A481) which listed assets of \$2,700,000 (A423). That letter simply lists certain assets Somekh owned on that date and cannot be distorted to suggest that there were no other assets, such as the Rite-Aid mortgage note sold in 1974 for \$175,000 (A423-424). Assets which had been liquidated prior to the date of the letter obviously would not be listed in it and there was no proper reason for the SEC to try to create a contrary impression.

sistent -- a decision which the SEC has been unable validly to defend.

Thus, while the Opinion below ruled that the sole question in which the minority shareholders had any interest was whether to accept the \$2.00 offering price or pursue their statutory right of appraisal (A20), the District Court illogically and erroneously concluded that somehow -- unexplained -- the question the minority shareholders had to decide was affected by the so-called "overriding purpose" for the merger. The "overriding purpose" for the merger could not affect the question which the minority shareholder had for decision, and neither the SEC nor the Court below have shown that it was. Indeed, the Court below never even found that the purpose to enable Somekh to repay his personal indebtedness was material under the federal securities laws. Obviously, it was not.

Finally, as has been seen, the District Court found no fault with the purpose of returning Parklane to private status disclosed in the Proxy Statement or the disclosure that, upon the merger, only the shareholders of the surviving corporation would be entitled to the benefit of all its assets. Instead, the Court below, to find actionable the purpose for the merger, relied upon the existence of the irrelevant and immaterial bank loans and found that the "overriding purpose" for the merger was to enable Somekh to repay those loans (A13).

The District Court never explained why the so-called "overriding purpose" was actionable under the federal securities laws. Nor, in light of the disclosure made in the Proxy Statement that the shareholders of the surviving corporation were entitled to the benefit of all the company's assets (A507), is there any rational explanation for finding that the non-disclosure of the "overriding purpose" was actionable. The "overriding purpose" was no more actionable than the purposes disclosed in the Proxy Statement. To find, as did the Court below, that non-disclosure of the so-called "overriding purpose" was a violation of the federal securities laws was plainly erroneous. This is to say nothing of the fact that the District Court made no finding that it was material.

III

The SEC has also mistakenly attempted to enlarge upon the ruling of the Court below that "the sole question facing a minority shareholder was whether to accept the \$2.00 per share price or to pursue his rights as a dissenting shareholder in an appraisal proceeding" (A20). It contends that there was a third alternative.

Though not even remotely suggested by the District Court, the SEC argues in its main (p. 24 n.20) and answering

(p. 12) briefs that had the Proxy Statement disclosed the purpose to enable Somekh to repay a personal indebtedness, the minority shareholders or others might have been able to enjoin the merger under state law and that, therefore, such disclosure was material. In this regard, the SEC has referred to Pecore v. Concord Fabrics, Inc., 83 Misc. 2d 120, 371 N.Y.S. (Sup. Ct.), aff'd, 50 App. Div. 2d 787, 377 N.Y.S. (1st Dep't 1975).

The argument is an obvious straw-man. The minority shareholders here had the benefit of the same disclosures on the basis of which the plaintiff in Concord Fabrics sought to enjoin the proposed merger. There, as here (A506), the proxy statement disclosed that the purpose of the proposed merger "'is to return the Company to the status of a privately - held corporation'". 371 N.Y.S.2d at 551.

Also, in substantially the language of the Proxy Statement here (A507), the proxy statement in Concord Fabrics, supra, disclosed that "'Upon consummation of the merger, the [majority shareholders] will be the sole stockholders and directors of the Company, and will thus be able to determine all policies of the Company, such as salaries for themselves and others, dividends and business activities, without public scrutiny and solely with regard to their own interests.'" 371 N.Y.S.2d at 551. (emphasis added)

Thus, the disclosures made in the Proxy Statement here afforded the additional alternative which the SEC contends Concord Fabrics, supra, provides. Since, however, all the disclosures necessary to provide the Concord Fabrics alternative appear in the Proxy Statement here, the non-disclosure of the "overriding purpose" found by the District Court was immaterial as a basis for a third alternative. Furthermore, even if there were such a third alternative, those disclosures were known to the minority shareholders when the Proxy Statement was issued.

IV

To support the erroneous claim that the Parklane Proxy Statement should have been amended to disclose a purported agreement at an October 4, 1974 meeting between Curtiss, the FRB representative, and Somekh, the SEC relies solely upon, and the District Court erroneously accepted, Curtiss' faulty recollection on direct examination of what transpired at that meeting. Upon the basis of that testimony alone, the SEC erroneously asserts that Somekh "agreed" to obtain assurances of cancellation of the Nassau Street leasehold from Parklane's two subtenants if Curtiss recommended a price of \$1,200,000, regardless of whether the FRB adopted the recommendation (SEC ans. br. 17).

The SEC's claim that there was such an agreement is untrue. Cross-examination of Curtiss and his October 7, 1974 letter to the FRB established (a) that Somekh had not

agreed to obtain such assurances from Parklane's subtenants merely on the basis of Curtiss' recommendation of \$1,200,000 and (b) that Somekh was to do nothing based upon Curtiss' recommendation alone. Somekh was not even to attempt to seek those assurances unless and until the FRB adopted Curtiss' recommendation and agreed to pay the amount recommended. These are precisely the facts Curtiss, in his October 7, 1974 letter (A573), reported to the FRB.

Thus, Curtiss, leaving no doubt as to the conditional nature of the discussion, wrote:

"Upon my advise [sic] to Mr. Somekh that \$1,200,000 will be paid he immediately will attempt to secure respective letters from Counsel [for the two subtenants] for a vacating of the two occupied premises by a date certain upon payment of the amounts stated." (A573)(emphasis added)

The District Court, in its Opinion, and the SEC, in its briefs, avoided that report, though, at trial, it was admitted in evidence, upon the SEC's offer, as the best evidence of the October 4 meeting. Mr. Ormsten of the SEC, in making the offer, proceeded as follows:

"Q Was that letter accurate and correct at the time that you [Mr. Curtiss] wrote it?

A It was.

MR. ORMSTEN: Your Honor, I respectfully submit that in some degree and in some respects Mr. Curtiss has not completely remembered all of the contents

of this letter and I submit it is a past recollection recorded and is the best evidence and offer it into evidence."
(A356)

Upon cross-examination, Curtiss confirmed that, as stated in his October 7 letter, Somekh was not to attempt to obtain assurances of cancellation from Parklane's subtenants unless Curtiss first obtained a commitment from the FRB to pay the amount Curtiss was to recommend (A414-415). Curtiss never obtained any such commitment (A403). Upon the basis of the proof provided by Curtiss alone, it was clear that no agreement was reached as the SEC's answering brief (p. 17) erroneously asserts.

With respect to the October 4 meeting, the SEC's answering brief compounds the demonstrated error in respect of the claimed agreement. The SEC asserts that Curtiss' testimony as to that meeting was contrary to that of Somekh, and that the Court below "chose to credit" Curtiss' testimony over that of Somekh (SEC ans. br. 17n.16). That assertion tends to mislead. The District Court did not credit Curtiss' testimony over that of Somekh. Rather, the significant error committed by the Court below was to credit Curtiss' direct testimony over Curtiss' corrected testimony on cross-examination and to disregard the conditional nature of the discussion had as reported by

Curtiss in his October 7 letter to the FRB.* It is precisely because the District Court unjustifiably made such a one-sided use of the proof provided by Curtiss that its finding as to the October 4 meeting is clearly erroneous. United States v. United States Gypsum Co., supra; Feder v. Martin Marietta Corp., supra.

The SEC's answering brief also erroneously contends that "the specifics of the [October 4] conversation" between Curtiss and Somekh "are irrelevant"; that only the fact that there was a conversation should be considered (SEC ans. br. 17n.16); and that the conversation, regardless of what was said, constituted "a significant change" in the status of the negotiations requiring amendment of the Proxy Statement (SEC ans. br. 19).

The contention thus made borders on the absurd. Obviously, the significance of a conversation cannot be considered without regard to what in fact was said. Here, as has been seen, the October 4 conversation was entirely conditional in nature. At the October 4 meeting, the answer

*Contrary to the impression which the SEC has sought to create, Somekh's testimony as to the October 4 meeting was completely consistent with that of Curtiss' testimony on cross-examination and Curtiss' October 7 report of that meeting (Ds' ans. br. 23-27). Thus, Somekh also confirmed the conditional nature of the discussion he had with Curtiss and that no valid basis exists for claiming an agreement as erroneously asserted by the SEC (Ds' ans. br. 25-27).

to the question whether the FRB would adopt Curtiss' \$1,200,000 recommendation was a complete unknown. The question was soon answered, and answered in the negative. In a telephone conversation between Curtiss and Somekh within a week of the October 4 meeting, Curtiss, as he testified, advised Somekh that he had made the recommendation; that the FRB had not acted upon it; and that the FRB had such serious construction cost problems in respect of the contemplated building "to the extent they may not even build it"* (A347). (emphasis added) In short, upon the basis of that telephone conversation, there were no reasonable grounds for believing that the FRB would ever adopt Curtiss' recommendation (Ds' main br. 28-30). The fact is that the recommendation never was adopted (A403).

Clearly, the October 4 meeting produced no change -- let alone a significant change -- in the status of the FRB-

*The SEC's answering brief (p. 18) attempts to create the erroneous impression that Curtiss reported that the FRB "were reevaluating their offer" and inexplicably cites, in that connection, defendants' main brief at page 28. There is no support for the erroneous assertion the SEC has thus made. There was then no offer to be reevaluated (Ds' main br. 26-31).

Even if the SEC's self-serving statement that the FRB was reevaluating the offer were true, it would only disprove the very argument the SEC urges. If it were true, it would confirm the obvious uncertainty, which in fact existed, whether Curtiss' recommendation would be adopted. It would also negate the SEC's statement that the "prospects for a successful transaction were good" (SEC ans. br. 21n.20). Curtiss' recommendation had no significance without approval by the FRB. That approval the FRB did not then or thereafter ever give (Ds' br. 26-31).

Parklane discussions between September 24, 1974, the date the Proxy Statement was issued, and October 14, 1974, the date of the Parklane shareholders' meeting at which the merger was approved (Ds' main br. 26-31). The disclosure in the Proxy Statement was that "there are no negotiations at present. The Company is unable to determine if another offer will be made." (A519) Upon the basis of the October 4 meeting and the subsequent telephone conversation, there was no conceivable reason to amend the Proxy Statement. The District Court's finding to the contrary could not be more clearly erroneous. It was only reached in disregard of relevant proof.

V

The SEC's answering brief (pp. 22-28) also unsuccessfully attempts to defend the District Court's finding that there were certain defects in one of the two appraisals made of the Parklane shares and that they were not disclosed in the Proxy Statement. Thus, on the basis of the District Court's finding, that brief asserts (a) that there was a failure to inform Russ of Thomson & McKinnon of certain information and (b) that such information was material. However, as the SEC's briefs themselves show, the SEC has been unable, as a matter of fact or law, to defend either

branch of that finding. As will hereinafter be seen, there was no such failure of disclosure and, even if there were, the information to which the finding below related was, on the record here, immaterial.

First, as to the claimed failure to disclose to Russ negotiations as to the possible cancellation of the FRB-Parklane lease, the SEC has clearly established that there were no negotiations to disclose.

It will be recalled that Thomson & McKinnon had been retained on August 12, 1974 to perform an appraisal and that it delivered its appraisal as of August 29, 1974 (Ds' main br. 38). During that period there were no negotiations for cancellation of the FRB-Parklane lease. The SEC itself has confirmed that between July and September 1974 there were no such negotiations and no indication that the FRB had any interest in cancellation of the lease. Thus, the SEC's main brief (pp. 9-10) states:

"[O]n June 27, 1974, Parklane made a counter-offer of \$1.2 million for the cancellation of the leasehold (A245). Although there was correspondence between Somekh and Curtiss about the counter-offer during July [1974], it expired without any action (A392).

"On September 29[sic], 1974, the time the proxy solicitation was originally prepared and filed with the Commission, the Nassau Street negotiations had apparently ceased and the proxy statement reflected that status." (emphasis added)

Since negotiations had ceased and there were none during the entire period of the preparation of the Thomson & McKinnon appraisal, there was obviously nothing to disclose in that regard and the question of materiality of any such non-disclosure was obviously non-existent. The District Court's finding to the contrary (A21-22), of necessity, was clearly erroneous.

Second, it was just as erroneous for the District Court to have found that the Proxy Statement was defective on the ground (a) that Russ was unaware of intended post-merger real estate transactions between Parklane and Somekh and (b) that such information was material (A17-18). The reason such an issue even arose is that Russ, called as a witness by the SEC, had obviously not had his recollection refreshed as to the testimony he had given during the SEC investigation -- testimony that, during the preparation of the Thomson & McKinnon appraisal, Somekh had informed him not only that he was considering such real estate transactions, but also that he was considering the use of Parklane's cash flow for that purpose.

Upon cross-examination, Russ, with his recollection refreshed, acknowledged that Somekh had told him that "if he could use the cash flow of Parklane, he might merge some of his real estate operations into the company after it

went private" (A313-314). (emphasis added) As Russ testified as a witness during the SEC's investigation, that information had no bearing on his appraisal (Ds' main br. 35).

Similarly, Frank Rubinstein of Foster Securities, Inc. the second of the two firms which had appraised the Parklane shares (Ds' main br. 39-40), testified in the course of the SEC's investigation as follows:

"...I was not as concerned with what he [Somekh] was going to do privately. I was more concerned with the fellow who had bought his stock and what he was going to get for it, not what Mr. Somekh was going to do." (A605, 617)

As to Russ, there can be no question, on the basis of his own testimony, but that he was aware that Somekh contemplated post-merger real estate transactions and the application in that regard of cash flow of Parklane, because Somekh had told him so (A313-314). Accordingly, in this regard, there was no valid reason for the SEC to claim, or the District Court to find, a failure of disclosure and a defect in the Proxy Statement. Russ, in the course of the Thomson & McKinnon appraisal, obviously had decided there was no need to pursue the matter. As to the appraisal he was making, it was an appraisal of the value of Parklane's shares as a "specialty retail" business -- the only kind of business in which the Parklane shareholders could have had any interest.

The SEC's attempt to defend the finding below of a defect in the Proxy Statement must fail for yet another reason. Neither the District Court nor the SEC has shown -- nor could they -- that post-merger real estate transactions had any materiality to either of the two appraisals made of the Parklane shares. As was seen in defendants' main brief (pp. 57-59), the District Court misconstrued the materiality test of TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438 (1976). Instead, it fashioned and applied its own demonstrably erroneous concept of materiality (A20-21).

The District Court held that if, by reason of a misstated or omitted fact, there were a substantial likelihood that the offering price for the Parklane shares would have been affected, upward or downward, to any degree -- no matter how miniscule or insignificant in amount -- such fact would be material. Obviously, however, if the amount were miniscule or insignificant, the Northway test of materiality could not possibly be satisfied. Under Northway, supra, the amount would have had to have been sufficiently great to have assumed "actual significance in the deliberations of the reasonable shareholder." 426 U.S. at 449. (emphasis added)

Upon the record here, it cannot conceivably be contended that post-merger real estate transactions had any materiality. The SEC, at trial, did not even remotely

attempt to prove the materiality of any such transactions. At the very most, Russ, on direct examination, testified that post-merger real estate transactions "would have affected the appraisal" (A308) -- a statement underlined in the lengthy quotation from Russ' direct examination which appears in the SEC's answering brief (pp. 24-25). However, upon the record before this Court, there is not a scintilla of evidence as to the extent or degree to which the appraisal or the offering price would have been affected had post-merger transactions been taken into account. Therefore, there was no basis upon which to conclude that the appraisal would have been affected to a degree which would have assumed, in the words of Northway, supra, "actual significance in the deliberations of the reasonable shareholder." 426 U.S. at 449. The SEC's utter failure of proof on the question of materiality is seen in the following telling testimony Russ gave on cross-examination:

"Q Sir, the Court inquired about the effect of the acquisition of land or real estate on cash flow.

If you were aware, sir, that cash flow would be used in respect of an investment in real estate, how would that have affected your appraisal, sir?

A It could have affected it -- it would really depend upon the fact of the situation. If the investment in the assets were producing more cash flow and more earnings, it possibly could have enhanced the evaluation.

If, on the other hand, the use of the cash flow were to show up an investment that was draining cash and was in an area where there wasn't much likelihood of the real estate regaining its economic viability, then it could have just as easily negatively affected the appraisal." (A312) (emphasis added)

Thus, even if post-merger real estate transactions were relevant, how Russ' appraisal may have been affected by them is a matter of sheer speculation upon the record here. In these circumstances, there is no way to say that post-merger real estate transactions would have had any material affect whatsoever upon the Thomson & McKinnon appraisal. Accordingly, the finding of the District Court as to materiality in this regard could not have been more erroneous.

The SEC's position, in its answering brief, is as erroneous as the finding made by the Court below. Each suffers from the same fundamental fallacy and the same lack of proof as to materiality.

Thus, the SEC erroneously states:

"If the independent appraisal indicated that a state appraisal would produce a higher figure than Parklane's \$2 offer, then resort to such proceedings was the advisable course; if an independent appraisal indicated a lower figure, it was unwise." (SEC ans. br. 26)

That statement does no more than beg the question of materiality. If the amount by which the \$2 offer might

have been higher or lower was miniscule or insignificant or unchanged, then it would be immaterial. On the record here, there is no proof to the contrary and no basis upon which the finding of the Court below can be defended against reversal.

VI

Finally, the SEC's answering brief asserts (a) that Parklane's annual report for the fiscal year ending September 28, 1974 and a quarterly report filed October 23, 1975 were deficient (p. 6n.6) and (b) that there are a "few reports" filed after September 29, 1974 which contain information about the merger and should be amended (p. 35n.32). The assertions are meaningless and are devoid of any support in the record. This is not a case of a District Court "failing to expressly specify each report," as urged by the SEC (SEC ans. br. 35n.32). Rather, since these reports were never even identified at the trial or offered in evidence, the District Court had no knowledge or information as to their contents and, therefore, had no basis for making any finding that would require any amendment of them (Ds' main br. 65-66).

Conclusion

It is respectfully submitted that the SEC did not

prove its case as a matter of fact or law; that the SEC was not entitled to any relief; and that the District Court should not have granted any relief. It is respectfully submitted further that the Judgment below (A30), to the extent defendants appealed therefrom (A595), should be reversed as a matter of fact and law.

Respectfully submitted,

JACOBS PERSINGER & PARKER
Attorneys for Defendants-
Appellants-Appellees
Parklane Hosiery Co., Inc.
and Herbert N. Somekh

IRVING PARKER
JOSEPH N. SALOMON
JEFFREY I. SLONIM

Of Counsel

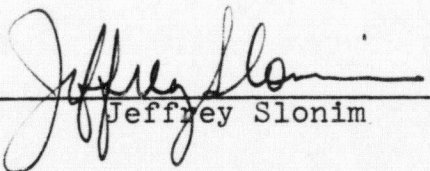
STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

JEFFREY SLONIM, being duly sworn, deposes and
says:

That he is not a party to the action, is over 18
years of age, and resides at 2815 Coyle Street, Brooklyn,
New York; and that on the 19th day of May, 1977, deponent
served the annexed Reply Brief upon

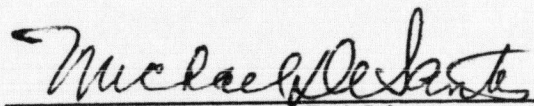
HARVEY L. PITT
General Counsel
Securities and Exchange Commission
 at
500 North Capitol Street
Washington, D.C. 20549

the address designated by said attorney for that purpose, by
depositing two true copies of the same enclosed in a postpaid
properly addressed wrapper in an official depository under
the exclusive care and custody of the United States postal
service within the State of New York.



Jeffrey Slonim

Sworn to before me this
19th day of May, 1977.



Notary Public
MICHAEL DeSANTIS
Notary Public, State of New York
No. 03-0930908
Qualified in Queens County
Commission Expires March 30, 1979